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No. 87-1841

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

CITY OF SANTA MONICA,
Petitioner,

vs.

SHELL OIL COMPANY,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION TO CROSS-PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Shell disagrees with cross-petitioner's statement of the questions presented. Shell believes the cross-petition presents only one issue:

> Whether conditions imposed by a city upon an interstate pipeline's use of the subsurface of public streets are subject to Commerce Clause scrutiny.

TABLE OF CONTENTS

Page

QUESTION PRESENTED

TABLE OF AUTHORITIES iii

PRELIMINARY STATEMENT 1

CONSTITUTIONAL PROVISIONS INVOLVED 2

STATEMENT OF THE CASE 3

REASONS FOR GRANTING OR DENYING THE PETITION 4

I. THE CITY OF SANTA MONICA AND ITS AMICI SEEK TO AMELIORATE THEIR FINANCIAL PROBLEMS BY IMPOSING FEES ON INTERSTATE COMMERCE 4

II. THE CITY ACTS AS A MARKET REGULATOR, NOT A MARKET PARTICIPANT, WHEN IT ISSUES FRANCHISES FOR PIPELINE USE OF CITY STREETS 5

A. The City Only Holds The Property In Question For Street Purposes, Not As Its Own Property To Do With As It Wishes. This Militates Against Application Of The Market Participant Doctrine And In Favor of Treating The City As A Regulator. 7

Page

B. The Market Participant Doctrine Has No Place Where The Governmental Entity Has Monopoly Power Over A Finite Resource. 9

CONCLUSION 13

TABLE OF AUTHORITIES

Page

Cases

Hughes v. Alexandria Scrap Corp.
426 U.S. 794, 49 L.Ed.2d 220,
96 S.Ct. 2488 (1976) 6

Jefferson County Pharmaceutical Association, Inc. v. Abbott Laboratories
460 U.S. 150, 74 L.Ed. 882,
103 S.Ct. 1011 (1983) 6

Kassel v. Consolidated Freightways Corp.
450 U.S. 662, 67 L.Ed.2d 580,
101 S.Ct. 1309 (1981) 11

Mervynne v. Acker
189 Cal.App.2d 558,
11 Cal.Rptr. 340 (1961) 7

Parker v. Brown
317 U.S. 341, 87 L.Ed. 315,
63 S.Ct. 307 (1943) 6

Raymond Motor Transportation, Inc. v. Rice
434 U.S. 429, 54 L.Ed.2d 664,
98 S.Ct. 787 (1978) 11

Reeves' Inc. v. Stake
447 U.S. 429, 65 L.Ed.2d 244,
100 S.Ct. 2271 (1980) 6

Page

South-Central Timber Development, Inc. v. Wunnicke
467 U.S. 82, 81 L.Ed.2d 71, 104 S.Ct. 2237 (1984) 2, 6

Southern Pacific Company v. Arizona
325 U.S. 761, 89 L.Ed. 1915, 65 S.Ct. 1515 (1945) 5

United States v. Aluminum Company of America
148 F.2d 416 (2nd Cir. 1945) 12

White v. Massachusetts Counsel of Construction Employers, Inc.
460 U.S. 204, 75 L.Ed.2d 1, 103 S.Ct. 1042 (1983) 6

Constitutions

United States Constitution
Commerce Clause 1, 2, 4-6, 11, 12
Art. 1, § 8, cl. 3 2
Supremacy Clause
Art. VI, cl. 2 3
Tenth Amendment 3

California Constitution
Article XIII A 4

Rules

Supreme Court Rules
Rule 28.1 2

Page

Statutes

California Public Utilities Code § 6202 8

Texts

10 E. McQuillan, *The Law of Municipal Corporations* (3d ed. 1978) § 30.40 ..... 7, 8

K. Ehrman & S. Flavin, *Taxing California Property* (2d ed. 1979) 4

Landes and Posner, *Market Power in Antitrust Cases*, 94 Harv.L.Rev. 937 (1981) 11, 12

1 R. Rotunda, J. Nowak & J. Young, *Treatise on Constitutional Law* (1988 Supp.) § 11.11 5

Rotunda, *The Doctrine of the Inner Political Check, the Dormant Commerce Clause, and Federal Preemption* (1986) 53 Transport. Pract. J. 263 5

L. Sullivan, *Handbook of the Law of Antitrust* 57 (1977) 11

L. Tribe, *American Constitutional Law* (2d ed 1988) § 6-5 5

Oil Pipelines of the United States: Progress and Outlook 15 (Assoc. of Oil Pipelines, 1983) 11

Page

R. Posner & F. Easterbrook, *Antitrust Cases, Economic Notes* and other materials (1981) 11

Turner, *Antitrust Policy* and the cellophane *Case*, 70 Harv.L.Rev. 281 (1956) 12

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BRIEF IN OPPOSITION TO CROSS-PETITION FOR WRIT OF CERTIORARI

PRELIMINARY STATEMENT

In its Cross-Petition, Santa Monica argues that the market participant exception to the dormant Commerce Clause applies in the case at bench. This argument is also championed — and the real reasons therefore made clear — by the City's three *amici*. Confronted with the effect of a California initiative measure that amended the California Constitution and limited local governments' power to levy taxes on their own citizens, the cities hope to collect additional fees from interstate commerce. They realize that the resulting Commerce Clause problems can be avoided if

Cities are held to be mere "market participants" and thus exempt from Commerce Clause scrutiny as they impose user fees for the use of the subsurface of city streets.

As some members of this Court and the City's *amici* have recognized, "the precise contours of the market participant doctrine have yet to be established . . . ." *South-Central Timber Development, Inc. v. Wunnicke*, 467 U.S. 82, 93, 81 L.Ed.2d 71, 104 S.Ct. 2237 (1984). (Plurality opinion.) Absent an opinion from this Court holding that they are constrained by the Commerce Clause when they impose user fees for the use of the subsurface of public streets, local governments will be encouraged to solve their local revenue problems by imposing excessive fees on interstate commerce.

Petitioner and cross-respondent Shell Oil Company ("Shell")[1] strongly urges the Court to grant the cross-petition in this case but for reasons different from those asserted by cross-petitioners. This petition should be granted but only in connection with a grant of the Petition for Writ of Certiorari in Case No. 87-1685 so that this Court can fully address the problem.

CONSTITUTIONAL PROVISIONS INVOLVED

Two provisions of the United States Constitution are relevant to this case:

1. The Commerce Clause, article I, section 8, clause 3:

> "The Congress shall have Power . . . to regulate Commerce . . . among the several States, ..."

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[1] Shell hereby incorporates by reference the List Pursuant to Supreme Court Rule 28.1, set forth at pages iii-x of its Petition for Writ of Certiorari in Case No. 87-1685.

2. The Supremacy Clause, article VI, clause 2:

> "This Constitution . . . shall be the supreme Law of the Land; . . . ."

Shell does not agree that this case raises issues under the Tenth Amendment to the United States Constitution.

STATEMENT OF THE CASE

Shell incorporates by reference the statement of the case contained in its Petition for Writ of Certiorari in Case No. 87-1685. In addition, Shell responds to two erroneous statements made by the City in its statement of the case:

First, Shell does *not* claim a right to lease the subsurface of city streets for a nominal fee. Shell claims a right, as recognized by this Court, to pay a reasonable fee to the City for the use of the subsurface of the streets.[2]

Second, Shell has never claimed any right tantamount to eminent domain, or claimed the power to appropriate a permanent exclusive right in the subsurface. Rather, Shell has maintained that its use is always subject to reasonable non-preempted regulation by the City. Shell has also recognized the possibility that in the future Santa Monica might be justified in refusing to renew the franchise if, for example, numerous other oil pipeline operators apply for franchises in the same location, or if the pipeline interferes with other proper street purposes (which it does not). *See*, Shell's Reply Brief in the Ninth Circuit, at 17.

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[2] *See*, Petition for Writ of Certiorari in Case No. 87-1685, section I.

REASONS FOR GRANTING OR DENYING THE PETITION

I.

THE CITY OF SANTA MONICA AND ITS AMICI SEEK TO AMELIORATE THEIR FINANCIAL PROBLEMS BY IMPOSING FEES ON INTERSTATE COMMERCE

The City's *amici* demonstrate the purpose behind the cities' desire to be free of Commerce Clause restraints when imposing user fees for the use of the subsurface of city streets. They point to a California tax reform initiative which has "greatly restricted the power of California cities to raise revenues by taxation." California Constitution, article XIII A.

The year 1978 saw the culmination of a "taxpayers' revolt" in California. This revolt was caused by a dramatic increase in the property tax burden placed on California homeowners. In the sixteen years prior to 1978, "assessed values in California tripled, tax rates increased by 51 percent, and property taxes themselves more than quadrupled." California voters enacted "Proposition 13," an amendment which added article XIII A to the State Constitution which limited the taxes assessed by local governments. K. Ehrman & S. Flavin, *Taxing California Property* (2d ed. 1979) pp. 28-32. Broadly speaking, article XIII A limits property taxes to one percent of a property's value at the date of acquisition plus an annual inflation factor of no more than two percent. In addition, it prohibits the imposition of new local special taxes except upon an affirmative vote of 2/3's of the electorate and prohibits any new local real property ad valorem taxes or any new sales taxes on the sale of real property.

By their use of the political process, the citizens of the various local cities are thus able to insulate themselves against local taxation. As a result, the cities themselves are encouraged to find means of raising revenues from entities, such as interstate pipeline operators, which are unrepresented in the local citizenry. Here, the Shell Oil Company pipeline is such a target.

Cases such as this, where the burden on interstate commerce is placed on an entity which is unrepresented in the local citizenry and where there is no local proxy that will effectively represent its interests, are particularly appropriate cases for Supreme Court review under the Commerce Clause. Without such review, the purposes of the Commerce Clause will be frustrated and "economic Balkanization" will result. *Southern Pacific Company v. Arizona*, 325 U.S. 761, 767-768 n. 2, 89 L.Ed. 1915, 65 S.Ct. 1515 (1945); L. Tribe, *American Constitutional Law* (2d ed. 1988) § 6-5 ; 1 R. Rotunda, J. Nowak & J. Young, *Treatise on Constitutional Law* (1988 Supp.) § 11.11; Rotunda, *The Doctrine of the Inner Political Check, the Dormant Commerce Clause, and Federal Preemption* (1986), 53 Transport. Pract. J. 263.

II.

THE CITY ACTS AS A MARKET REGULATOR, NOT A MARKET PARTICIPANT, WHEN IT ISSUES FRANCHISES FOR PIPELINE USE OF CITY STREETS

When Santa Monica issues a franchise for pipeline use of the City streets, it is acting as a market regulator, not a market participant.

Cases decided by this Court establish a distinction between state and local governments acting as "regulators,"

and state and local governments acting as "market participants." *White v. Massachusetts Counsel of Construction Employers, Inc.*, 460 U.S. 204, 75 L.Ed.2d 1, 103 S.Ct. 1042 (1983); *Reeves' Inc. v. Stake*, 447 U.S. 429, 65 L.Ed. 2d 244, 100 S.Ct. 2271 (1980); *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 49 L.Ed.2d 220, 96 S.Ct. 2488 (1976). *See also, South-Central Timber Development, Inc. v. Wunnicke*, 467 U.S. 82, 81 L.Ed. 2d 71, 104 S.Ct. 2237 (1984). When local governments act as "market participants," they are not subject to Commerce Clause scrutiny. When they act as "regulators," they are.

The distinction between acting as "regulators" and acting as "market participants" is nothing more than a common sense recognition that from time to time state or local governments depart from their traditional roles as governmental bodies and engage as business people in the market place. When they are in their governmental role, we call them "regulators" and they are governed by the rules applicable to governments. On the other hand, when they engage as business people in the market place, we refer to them as "market participants" and they are then governed by the rules applicable to business people and not by the rules applicable to governments. For example, the antitrust laws apply to a state when it is acting as a market participant but not when it is acting in its governmental capacity. In this regard, *see Jefferson County Pharmaceutical Association, Inc. v. Abbott Laboratories*, 460 U.S. 150, 154, 74 L.Ed.2d 882, 103 S.Ct. 1011 (1983)(where it was held that state action immunity under the antitrust laws does not apply where a state has chosen to compete in the private retail market). Also, *see Parker v. Brown*, 317 U.S. 341, 350-352, 87 L.Ed. 315, 63 S.Ct. 307 (1943)(where it was held that when the state acts as a market regulator, it is immune from antitrust scrutiny).

In the case at bench, the City of Santa Monica is acting as a regulator and not as a market participant.

A. The City Only Holds The Property In Question For Street Purposes, Not As Its Own Property To Do With As It Wishes. This Militates Against Application Of The Market Participant Doctrine And In Favor Of Treating The City As A Regulator.

Here, the City of Santa Monica seems to base its argument that it is a market participant on the theory that it "owns" the streets. This is certainly not the case. All cities, Santa Monica included, hold streets in trust for the public, for street purposes. This rule is stated in *Mervynne v. Acker*, 189 Cal.App.2d 558, 561, 11 Cal.Rptr. 340 (1961):

> ". . . Public highways belong to all the people of the state. Every citizen has the right to use them, subject to legislative regulation. . . ."

The same rule is stated by McQuillen:

> ". . . Whatever may be the quality or quantity of the estate of the city in its streets, that estate is essentially public and not private property, and the city in holding it is considered the agent and trustee of the public and not a private owner for profit or emolument. . . ."

10 E. McQuillen, *The Law of Municipal Corporations* (3d ed. 1978), § 30.40 at 685. Not only are streets held in trust for public use, but the public use is that of the entire public, not just the municipality where the streets are located. Thus, McQuillen states at page 686:

> ". . . 'Streets are for the public use, but do not exist for the use of the municipality in which they are situated alone or its inhabitants.'. . . ."

Elsewhere, at pages 762-763 in Section 30.73, McQuillen elaborates further:

> ". . . The streets and public ways of a municipal corporation are held by it in trust for the public, to be used for the ordinary purposes of travel and such other uses as customarily pertain thereto *which, in recent years, are numerous and various.* . . ." (Emphasis supplied.)

There is no doubt that pipelines are proper and accepted street uses in California. The City cannot reasonably dispute that pipelines are commonly found in the subsurface of the City streets. For example, both Shell's pipeline and the local gas utility pipeline utilize the subsurface of the city streets in Santa Monica. Furthermore, California Public Utilities Code section 6202 acknowledges that oil pipeline uses are proper street purposes:

> "The legislative body of any municipality may grant a franchise . . . to use, or to lay and use, pipes and appurtenances for transmitting and distributing oil . . . ."

The City of Santa Monica does not own the streets in fee. It merely owns an easement for street purposes. C.R. 80:52. Thus, whether the City purports to be controlling the surface of the city streets or the subsurface of the city streets, its only title is for "street purposes." Nevertheless, the City clearly purports to not only exercise control over the surface of the streets but also control over the subsurface. It thus exercises the power to franchise the use of the subsurface of city streets for pipeline purposes. Indeed, the City has done so for many, many years as have virtually all other cities and counties in the State of California. It follows that pipeline usage of streets is a valid and accepted street use. Were that not so, cities would be powerless to grant pipeline franchises.

The City is, therefore, not dealing with its own property as a market participant when it grants franchises for pipeline purposes. It is dealing with public property which it holds in trust for all members of the public who, subject to reasonable regulation, are all entitled to reasonable use of the streets for proper street purposes. In short, the City is *regulating* the use of the streets.

B. The Market Participant Doctrine Has No Place Where The Governmental Entity Has Monopoly Power Over A Finite Resource.

Application of the market participant doctrine assumes that the governmental entity involved is simply one of many participants in the market_ place. It has no rational application where the governmental entity has monopoly power over a finite resource. The City of Santa Monica acknowledges this rule at page 6 of its Cross-Petition.

Here, the City of Santa Monica has a practical monopoly over pipeline routes within the City (a finite resource) because there is no viable alternative pipeline right of way for Shell other than the subsurface of the streets. In heavily urbanized areas, one cannot run a pipeline without making use of the city streets. In such areas, ownership of private land is so widely distributed and the parcels are so intensely developed that it is virtually impossible to assemble a pipeline right of way without using the city streets. Furthermore, even if a sufficient number of contiguous private parcels could be assembled, it would still be necessary to cross under public streets at the end of each city block. Public streets, therefore, are quite unique, indispensable and finite when it comes to subsurface pipeline transportation.

Although Santa Monica asserts that it does not have monopoly power over Shell, that is not the case. The City

does have monopoly power over Shell in a number of ways. First, it straddles and divides the 82.2 mile pipeline that stretches from Ventura to Shell's Wilmington refinery, near Long Beach, California. The cost to relocate the pipeline segment that runs through the City to a route outside of Santa Monica, if such relocation were possible, is approximately $2,500,000, exclusive of right of way acquisition costs. C.R. 80:64-66. Thus, when the City "competes" in the right of way market (assuming there really is such a "market"), it enjoys a $2,500,000 bargaining advantage over its "competitors." Such an advantage clearly gives the City market control and, thus, a practical monopoly up to $2,500,000.

This monopoly could not be broken by Shell's attempting to move its oil by tank truck or marine tanker or barge. To begin with, it is not economically feasible to move the oil by truck. At the present through-put rate of the subject pipeline, approximately 170 tanker trucks per day would be needed to transport the oil at a cost increase of approximately $1.36 per barrel. C.R. 80:45-46. Assuming 30,000 barrels of crude oil per day, simple mathematics show that the additional annual cost of such a project would be approximately $14,892,000. Furthermore, shipping the oil from Ventura by barge or marine tanker would simply not be feasible because of the lack of facilities located near the refinery that can handle the size and type of tanker which can be loaded with crude oil at Ventura. C.R. 80:46-47. Shell could not make arrangements to hire an existing public utility pipeline to carry Shell's oil for a fee even though the City of Santa Monica suggests that it could. There is absolutely no evidence in the record of the existence of any such public utility pipeline and — in fact — there are no such lines between Ventura and Wilmington.

In truth, these alternatives are not really alternatives at all. Oil pipelines are the safest mode for transporting

petroleum, one thousand times safer than trucks. *Oil Pipelines of the United States: Progress and Outlook* 15 (Assoc. of Oil Pipelines, 1983). Oil pipeline transportation charges are extremely low. *Id.* at 8, 16. Pipelines are "the most economical means of moving large volumes of petroleum overland for long distances . . . ." *Id.* at 2. Santa Monica's actions in this case and its argument that the market participant exception applies, ignores these facts and refers to "alternatives" without recognizing that those other modes of transportation are *not* reasonable substitutes for pipelines, and that the moving of an oil pipeline, when possible, is extremely expensive.[3]

The City, therefore, does have absolute power over the "price" charged for the franchise, at least up to the point where the franchise fee makes unreasonable and uneconomical alternatives attractive. This is a powerful demonstration of the City's monopoly power over Shell. *See*, R. Posner & F. Easterbrook, *Antitrust Cases, Economic Notes*, and other materials 360-362 (1981); L. Sullivan, *Handbook of the Law of Antitrust* 57 (1977); Landes and

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[3] The Commerce Clause is concerned with increased costs of transportation caused by state or local governments. In *Raymond Motor Transportation, Inc. v. Rice*, 434 U.S. 429, 438-439, 445-446, 54 L.Ed.2d 664, 98 S.Ct. 787 (1978), the Court struck down a state statute that forced a truck carrier to use different types of trucks within the state than those normally used by the carrier or to use the desired trucks in a different manner. In part, the *Raymond* court was concerned with the substantial increase in cost to move goods in interstate commerce which resulted from the operation of the statute. Another case is *Kassel v. Consolidated Freightways Corp.*, 450 U.S. 662, 674, 686, 67 L.Ed.2d 580, 101 S.Ct. 1309 (1981)(State law forced change in manner of transporting goods in interstate commerce; law added approximately $12,600,000 to the costs of all trucking companies doing business in state. Approximately $2,000,000 of that increase was borne by Consolidated. The Court also pointed out that interstate commerce could not be forced to bypass the state.).

Posner, *Market Power in Antitrust Cases*, 94 Harv.L.Rev. 937, 960-961 (1981); Turner, *Antitrust Policy* and the cellophane *Case*, 70 Harv.L.Rev. 281 (1956). As Judge Learned Hand recognized: "There are indeed limits to . . . power; substitutes are available for almost all commodities, and to raise the price enough is to evoke them." *United States v. Aluminum Company of America*, 148 F.2d 416, 425-426 (2d Cir. 1945).

The Ninth Circuit clearly recognized that because here traditional transportation corridors were involved and because of the City's practical monopoly power with respect to those transportation corridors, the City was not a market participant but instead was a regulator subject to scrutiny under the Commerce Clause. Ordinarily, that would be a sufficient basis for denying the City's Cross-Petition. The fact, however, that the City of Santa Monica (supported by its three *amici* cities) seeks to apply the market participant doctrine as a means of avoiding Commerce Clause scrutiny in its efforts to collect additional fees from interstate commerce is a sound reason for this Court's granting certiorari in both Case No. 87-1685 and in this case. It is important that this Court make it clear that under *no* theory may cities use their control over the subsurface of city streets to exact tribute from the interstate transport of commodities via subsurface pipelines.

CONCLUSION

For all the above reasons, this Court should grant certiorari in this case, but for reasons different than those asserted by the City of Santa Monica and its *amici*. Instead, the cross-petition should be granted but only in connection with the petition in Case No. 87-1685 so that this Court can fully consider the burden imposed on interstate commerce by the City's actions.

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Respectfully submitted,

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